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C O N F I D E N T I A L SECTION 01 OF 02 BEIJING 000760

SIPDIS

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SUBJECT: CURRENCY SWAP PLAN SHOWS RIVALRY, COOPERATION
BETWEEN CHINA, JAPAN, KOREA

REF: A. 2008 BEIJING 4121
[1](#)B. 2008 SINGAPORE 947
[1](#)C. 2008 SINGAPORE 143

Classified By: Economic Minister Counsellor Robert S. Luke. Reasons 1.4
(b) and (d).

SUMMARY

[1](#)1. (C) Japanese and Korean Embassy officials in Beijing agreed that ASEAN 3 currency swaps agreement remains more show than substance, despite the February 22 announcement by ASEAN 3 (China, Korea, Japan) Finance Ministers that the Multilateral Chiang Mai Initiative (CMIM) fund will be increased from USD80 billion to USD120 billion. Key questions about the operation of the swap agreements remain unanswered. China and Japan appear to be vying for leadership and influence while Korea reports that it often mediates between the two. According to a Beijing-based Japanese diplomat, Japan objects to China,s push to include Hong Kong as a separate member in the arrangement, assessing that inclusion is designed to strengthen China,s hand in the group. This diplomat also report that several participants are seeking to be selected as the host of the swap agreement,s future surveillance office in order to build expertise and to position themselves for a key role in any future regional finance initiatives. End Summary.

Background on Swap Agreement

[1](#)2. (SBU) On February 22, Finance Ministers from the ASEAN 3 countries -- which includes members of the Association of Southeast Asian Nations, plus China, Japan, and Korea -- announced that they would increase the value of currency swap agreements designed to mitigate short-term balance of payments issues to US\$120 billion from the previously announced US\$80 billion. In a March 6 meeting with Econoffs, Japanese Embassy Financial and Economic Affairs Counselor Satoru Shibata said funding issues had largely been agreed upon. China, Japan and Korea would provide 80 percent of the funds, or US\$96 billion, and ASEAN nations would contribute the remaining 20 percent. Of the \$96 billion, he said Japan would fund approximately 60 percent, or US\$58 billion, while China and Korea would split the remaining 40 percent, or US\$19 billion each.

Little Progress to Make the Agreement a Reality

13. (C) Apart from allocating the contributions, Shibata said, little progress has been to operationalize the agreement. Korean Embassy Finance and Economic Minister-Counselor (M/C) Yoo Kwangyeol offered a similar view in a March 13 meeting with the Embassy's Financial M/C and Econoff. Yoo said that the details of the ASEAN 3 agreement have not been worked out and will be complicated by China's cumbersome capital controls. He said actively using the money will be complicated and take time, and that Chinese, Korean, and Japanese financial experts were currently examining the issues. Yoo added that Japan and China had been jockeying to make the biggest contribution to the fund.

Swaps Designed to Facilitate Trade and Reassure Markets

13. (C) On the separate RMB/Won swap agreement between the Peoples Bank of China and the Bank of Korea, which is outside the framework of the CMIM, Korean M/C Yoo added that from Korea's vantage point, these bilateral swaps are not designed to support banks, but to facilitate RMB-denominated trade and reassure markets. He added that Korean banks have a limited presence in China and keep most of their assets and liabilities in U.S. dollars, not "renminbi." He noted that, after Chinese banks pulled RMB credit lines in October and November 2008 following Lehman Brothers' collapse, Korean banks in China had regained access to the interbank RMB market and that China's banking system had excess RMB

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liquidity and was loaning some of the excess funds to Korean banks in China.

Disagreement Over Hong Kong, Surveillance Unit Location

14. (C) Japanese Counselor Shibata highlighted Japan's disagreement with China over Hong Kong inclusion as a separate economy in the CMIM. He said Japan and other ASEAN nations are opposed and cannot understand why China is taking a hard-line stance on the issue. Hong Kong is not a member of the International Monetary Fund (IMF), which is "deeply linked" to the CMIM. Shibata believes China is seeking to gain more influence in the CMIM process by including Hong Kong. Korean M/C Yoo said Korea favors adding any economies that play a key role in Asia's financial system, including Hong Kong.

15. (C) Shibata added that another issue dividing the parties is the location of the swap agreement's surveillance office. He said Korea, Japan, and China are all seeking to have the surveillance unit located in their countries. In addition, he added, there remain unresolved questions about how to staff the unit and how the unit would interact with member countries. Korean M/C Yoo disagreed, saying Korea did not see the surveillance unit's location as a key issue because there is no timetable to establish the office.

16. (C) Perhaps because of the numerous issues outstanding, Japanese Counselor Shibata was non-committal regarding the likelihood of reaching an agreement on the CMIM by the next ASEAN 3 meeting in Bali on May 10, 2009, as planned.

COMMENT

17. (C) While not wanting to be seen as undermining Asian financial integration, China's support for the CMIM appears to remain lukewarm, as it sees this as a Japanese-led initiative. Spurred by the establishment of bilateral currency swaps between the Federal Reserve and Korea and Singapore, China has put much more emphasis on establishing its own bilateral swaps outside of the CMIM framework with

Hong Kong, Korea, Malaysia, and Belarus. These bilateral swaps are almost equal the size of the CMIM swaps, and unlike the CMIM swaps, have actually been used (with Hong Kong). PBOC officials have told us previously that China principally values the CMIM as the basis for a potential Asian Monetary Fund alternative to the IMF in the event China is unable to secure a satisfactory reallocation of voting shares within the IMF.

PICCUTA